

Sales of service that are accompanied with the transfer of tangible personal property are subject to liability under the Service Occupation Tax Act. See 86 Ill. Adm. Code 140.101. (This is a GIL).

March 5, 2003

Dear Xxxxx:

This letter is in response to your letter to the Department of December 3, 2002. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120 subsections (b) and (c), which can be found at <http://www.revenue.state.il.us/Laws/regs/part1200/>.

In your letter, you have stated and made inquiry as follows:

I have a question regarding the taxability of services. I have a client based in STATE who is starting a marine surveying & consulting business. As a marine surveyor, my client will be doing appraisals and inspections. He will be working with buyers and insurance companies to make sure the boat(s) is(are) sea worthy. He will mainly be dealing with yachts and small crafts. What he will be selling to his clients is his report. Some of his work will be performed in the state of Illinois. Thus, my question: is all or part of this type of work subject to Illinois sales tax? If yes, please send us the Illinois statutes that state that it is subject to sales tax, and the forms necessary to apply for an Illinois seller's permit.

If you are in need of additional information, please feel free to contact me.

Thank you for your assistance.

We hope that the following information regarding nexus and the Service Occupation Tax will be helpful.

Whether a retailer is subject to Illinois Retailers' Occupation Tax (sales tax) liability or is required to collect Illinois Use Tax from its Illinois customers depends upon whether that retailer has sufficient "nexus" with the State of Illinois so that the retailer will be subject to Illinois law. The following information outlines the principles of nexus.

An "Illinois Retailer" is one who either accepts purchase orders in the State of Illinois or maintains an inventory in Illinois and fills Illinois orders from that inventory. The Illinois Retailer is then liable for Retailers' Occupation Tax on gross receipts from sales and must collect the corresponding Use Tax incurred by the purchasers.

Another type of retailer is the retailer maintaining a place of business in Illinois. The definition of a "retailer maintaining a place of business in Illinois" is described in 86 Ill. Adm. Code 150.201(i), enclosed. This type of retailer is required to register with the State as an Illinois Use Tax collector. See 86 Ill. Adm. Code 150.801, enclosed. The retailer must collect and remit Use Tax to the State on behalf of the retailer's Illinois customers even though the retailer does not incur any Retailers' Occupation Tax liability.

The United States Supreme Court in *Quill Corp. v. North Dakota*, 112 S.Ct. 1904 (1992), set forth the current guidelines for determining what nexus requirements must be met before a person is properly subject to a state's tax law. The Supreme Court has set out a 2-prong test for nexus. The first prong is whether the Due Process Clause is satisfied. Due process will be satisfied if the person or entity purposely avails itself or himself of the benefits of an economic market in a forum state. *Quill* at 1910.

The second prong of the Supreme Court's nexus test requires that, if due process requirements have been satisfied, the person or entity must have physical presence in the forum state to satisfy the Commerce Clause. A physical presence is not limited to an office or other physical building. Under Illinois law, it also includes the presence of any agent or representative of the seller. The representative need not be a sales representative. Any type of physical presence in the State of Illinois, including the vendor's delivery and installation of his product on a repetitive basis, will trigger Use Tax collection responsibilities. Please refer to *Brown's Furniture, Inc. v. Zehnder*, 171 Ill.2d 410 (1996).

The final type of retailer is the out-of-State retailer that does not have sufficient nexus with Illinois to be required to submit to Illinois tax laws. A retailer in this situation does not incur Retailers' Occupation Tax on sales into Illinois and is not required to collect Use Tax on behalf of its Illinois customers. However, the retailer's Illinois customers will still incur Use Tax on the purchase of the out-of-State goods and have a duty to self-assess their Use Tax liability and the customer must remit the amount directly to the State. The Use Tax rate is 6.25%

In general, the imposition of the various local sales taxes in Illinois takes effect when "selling" occurs in a jurisdiction imposing a tax. The Department's opinion is that the most important element of selling is the seller's acceptance of the purchase order. Consequently, if a purchase order is accepted in a jurisdiction that imposes a local tax, that tax will be incurred. See 86 Ill. Adm. Code 270.115(b), enclosed. The tax rate is fixed by the location of the seller, not the delivery location. The fact that the item being sold is shipped from out-of-State or from another Illinois location is immaterial for purposes of local taxes if the sale occurs through order acceptance in an Illinois jurisdiction imposing a local tax. For these transactions the local tax will be incurred.

If a purchase order is accepted outside the State, but the property being sold is located in an inventory of the retailer which is located in an Illinois jurisdiction that has imposed a local tax (see, for example, Section 270.115(b)(3)), then the location of the property at the time of sale will determine where the seller is engaged in business for the purpose of determining the imposition of applicable local sales taxes. In situations in which the retailer has nexus, but both the purchase order acceptance and the location of the property being purchased are outside of the State of Illinois, such sales would only be subject to the Illinois Use Tax at the rate of 6.25%.

Although the regulation cited above (86 Ill. Adm. Code 270.115) deals with the municipal home rule taxes, the principles outlined in this regulation apply to all local taxes administered by the Department.

The sale of planning or consulting services that is accompanied with the transfer of tangible personal property such as reports is subject to liability under the Service Occupation Tax Act. Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred as an incident of their sales of service in Illinois. Servicemen incur either Service Occupation Tax (SOT) liability or Use Tax liability in these transactions. The tax consequences depend upon the method used to calculate the liability.

Servicemen may calculate their tax base in one of four ways: 1. Separately stated selling price; 2. 50% of serviceman's entire bill; 3. SOT on his cost price if he is a registered de minimis serviceman; or, 4. Use Tax on his cost price if he is an unregistered de minimis serviceman. Please see the enclosed copy of 86 Ill. Adm. Code 140.101, the Basis and Rate of the Service Occupation Tax.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of the sale of service. The tax is then calculated on the separately stated selling price of the tangible personal property transferred. If the servicemen do not separately state the selling price of the tangible personal property transferred, they must use 50% of the entire bill to the service customer as the tax base. Both of the above methods provide that in no event may the tax base be less than the servicemen's cost price of the tangible personal property transferred. Such servicemen collect a corresponding amount of Service Use Tax from their customers.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may qualify as de minimis if they determine that the annual aggregate cost price of tangible personal property transferred as an incident of the sale of service is less than 35% of the total annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphics arts production). Servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis. Registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon their cost price of tangible personal property transferred incident to the sale of service. Such servicemen should give suppliers resale certificates and remit Service Occupation Tax using the Service Occupation Tax rates for their locations. Such servicemen collect a corresponding amount of Service Use Tax from their customers.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Such de minimis servicemen handle their tax liability by paying Use Tax to their suppliers. If their suppliers are not registered to collect and remit tax, the servicemen must register, self-assess and remit Use Tax to the Department. The servicemen are considered to be the end-users of the tangible personal property transferred incident to service. Consequently, they are not authorized to collect a "tax" from the service customers.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

Martha P. Mote
Associate Counsel

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Enc.